



OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

Postal Service Retirement Benefits Benchmarking

WHITE PAPER

Report Number
HR-WP-14-002-DR

May 1, 2014





OFFICE OF INSPECTOR GENERAL

UNITED STATES POSTAL SERVICE

Executive Summary

*At the request of the
Postal Service, we benchmarked
its retirement benefits against
six private and two government
sector programs.*

The U.S. Postal Service continues to experience financial challenges and operated at a \$5 billion deficit in fiscal year (FY) 2013. The Postal Service remains a labor-intensive organization; it incurred about \$47 billion in compensation and benefits expenses¹ in FY 2013, including about \$6 billion for retirement benefits. In its 2013 Annual Plan, the Postal Service said it needs to create a new retirement plan for future employees as part of its efforts to gain control over personnel costs. At the request of the Postal Service, we benchmarked its retirement benefits against six private and two government sector programs.

In response to rising pension debt and difficulty in making promised pension payments, private and some state and local governments have adjusted their retirement benefit programs. However, federal employee retirement benefits have generally remained unchanged since the Federal Employees Retirement System (FERS) was enacted on January 1, 1987.

Federal law² requires that all federal employees, including Postal Service employees, be covered by one of two government-sponsored retirement plans: the Civil Service

Retirement System (CSRS)³ or FERS. Both are administered by the Office of Personnel Management. Federal law⁴ also requires that compensation and benefits of Postal Service employees be comparable to those of private sector employees. However, unlike private sector companies, federal agencies, including the Postal Service, do not have the authority to change retirement benefits for their employees.

The Civil Service Retirement Act of 1920 created CSRS for federal employees. It was replaced by FERS for federal employees hired on or after December 31, 1983.⁵ CSRS is a defined benefit,⁶ contributory retirement system that provides a basic annuity upon retirement. CSRS employees may also receive credit for unused sick leave but do not earn Social Security benefits. They may increase their retirement benefits by voluntarily contributing to a savings account or to the Thrift Savings Plan (TSP).⁷ There is no government contribution, but employee contributions are tax-deferred.

¹ Compensation and benefits expenses consist of salaries and wages, future retirement benefits earned in current periods, health benefits, plus miscellaneous other expenses incurred on behalf of current employees. All expenses of the retirement programs, except for retiree health benefits, are included in compensation and benefits expenses.

² Title 39 U.S.C. § 1005(d)(1).

³ This includes Dual CSRS, a subset of the CSRS plan. Employees with prior U.S. government service who were rehired between January 1, 1984, and January 1, 1987, are covered by Dual CSRS, which consists of a basic annuity and Social Security benefits.

⁴ Title 39 U.S.C. § 1003(a).

⁵ FERS was effective on January 1, 1987. However, federal employees hired between 1984 and 1986 were automatically converted to FERS in 1987.

⁶ A defined benefit plan promises a specified monthly benefit at retirement.

⁷ CSRS employees may increase their annuity by contributing up to 10 percent of their pay to a voluntary contribution account. The TSP is a retirement savings and investment plan established by Congress in the Federal Employees' Retirement System Act of 1986.



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Although the Postal Service's retirement benefits are comparable in many ways to those offered in the private sector, some differences exist.

FERS provides benefits from three sources: a basic benefit plan similar to that under CSRS, Social Security, and TSP. The TSP part of FERS is a defined contribution plan.⁸ Employing agencies automatically establish a TSP account for each FERS employee and contribute either 1 or 3 percent of salary to that account depending on the employee's hire date.⁹ FERS employees can also voluntarily contribute to their TSP account and employing agencies match those contributions.¹⁰ The retirement income from TSP depends on how much a participant and his or her employing agency contribute to accounts during working years and the earnings accumulated over that time.

Currently, of about 484,000 Postal Service career employees, about 50,000 participate in CSRS and about 434,000 participate in FERS.¹¹ About half of the CSRS participants contribute to TSP and about 80 percent of FERS participants contribute to TSP. TSP contribution rates among Postal Service employees average between 4 and 4 1/2 percent of pay. Newly hired federal employees who already have tax-deferred money in a traditional individual retirement arrangement¹² or another eligible

employer plan can transfer those accounts into their TSP. Conversely, workers who leave the federal government can transfer their TSP funds on a tax-deferred basis into another tax-qualified retirement savings account.

Overall, pensions, which were originally intended to attract and retain talented employees, are a major cost to organizations. As workers become more mobile and transient throughout their careers, many organizations are adjusting their retirement benefits programs to cater to an evolving workforce and putting the employee in control of his or her financial future. These organizations are also freeing themselves of long-term retirement costs by shifting the responsibility to the employee.

Although the Postal Service's retirement benefits are comparable in many ways to those offered in the private sector, some differences exist. All eight benchmarked organizations historically had defined benefit pension plans. However, seven benchmarked organizations transitioned, at least partially, to a defined contribution retirement benefits plan. The one remaining organization maintained a traditional defined benefit pension plan but increased the retirement age requirement, decreased employee benefits, and offered a delayed compensation plan.¹³

⁸ A defined contribution plan is where the employee and/or the employer contribute to the employee's individual account.

⁹ CSRS participants must make a contribution to establish a TSP account. It is not automatic and employing agencies do not contribute.

¹⁰ FERS participants receive employing agency matching contributions on the first 5 percent of pay contributed. The first 3 percent is matched dollar-for-dollar; the next 2 percent is matched 50 cents on the dollar.

¹¹ As of March 7, 2014. Career employees receive full employee benefits and privileges.

¹² A personal savings arrangement that allows employees to set aside money for retirement.

¹³ This is an alternate retirement savings vehicle that allows employees to set aside additional pretax retirement savings. While there is no match, upon retirement employees can access their individual contributions in addition to their pension payments.



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The Postal Service should consider the common practices, used by the organizations we examined, if it changes its retirement benefits.

Benefits constitute a larger share of compensation for federal workers, accounting for 39 percent of total compensation, compared with 30 percent in the private sector. As such, benefits help attract and maintain staff in the federal workforce. The Postal Service's retirement expense was about 12 percent of total annual compensation and benefits expenses in FYs 2011 through 2013. In the private sector, retirement and savings benefits average 3.7 percent of total compensation and benefits costs. For state and local governments, retirement and savings benefits average 9.4 percent.¹⁴

We identified common practices involving cost-savings, governance and administration, union negotiation and relations, and employee satisfaction strategies. The Postal Service should consider these practices, used by the organizations we examined, if it changes its retirement benefits.

¹⁴ U.S. Bureau of Labor Statistics Economic News Release, *Employer Costs for Employee Compensation*, March 12, 2014.

Transmittal Letter

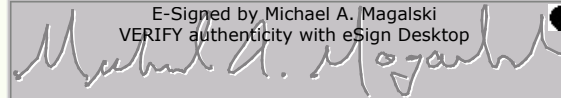


OFFICE OF INSPECTOR GENERAL
UNITED STATES POSTAL SERVICE

May 1, 2014

MEMORANDUM FOR: JEFFREY C. WILLIAMSON
CHIEF HUMAN RESOURCES OFFICER AND
EXECUTIVE VICE PRESIDENT

E-Signed by Michael A. Magalski
VERIFY authenticity with eSign Desktop



FROM: Michael A. Magalski
Deputy Assistant Inspector General
for Support Operations

SUBJECT: White Paper — Postal Service Retirement Benefits
Benchmarking (Report Number HR-WP-14-002-DR)

Attached are the results of our benchmarking review of U.S. Postal Service Retirement Benefits (Project Number 13YG030HR000). Retirement benefits are a significant component of the Postal Service's personnel costs. This white paper provides benchmarking results with six private sector companies and two public sector organizations and includes common practices used to implement benefit changes.

If you have any questions or need additional information, please contact Lorie Nelson, director, Human Resources and Support, or me at 703-248-2100.

Attachment

cc: Corporate Audit and Response Management

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Observations

The Postal Service remains a labor-intensive organization; it incurred more than \$47 billion in compensation and benefits expenses in FY 2013, including about \$6 billion for retirement benefits.

Introduction

The U.S. Postal Service continues to experience financial challenges and operated at a \$5 billion deficit in fiscal year (FY) 2013. This was the 7th consecutive year the Postal Service netted a financial loss. The Postal Service remains a labor-intensive organization; it incurred more than \$47 billion in compensation and benefits expenses in FY 2013, including about \$6 billion for retirement benefits. In its 2013 Annual Plan, the Postal Service said it needs to create a new retirement plan for future employees as part of its efforts to gain control over personnel costs.

A retirement benefits program is conceptualized as an employee's entitlement upon retiring from an organization or company. It is part of an overall compensation and benefits package that also can include leave and paid holidays, insurance, and disability. Federal law¹⁵ requires all federal employees, including Postal Service employees, to be covered by either the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (FERS). The Postal Accountability and Enhancement Act of 2006 also maintained the Postal Reorganization Act's requirement that postal employees receive compensation comparable to employees in the private sector.¹⁶ However, unlike private sector companies, the Postal Service does not have the authority to change retirement benefits for its employees.

CSRS was established in 1920 and covers employees hired before January 1, 1984. Participants do not pay Social Security payroll taxes, and they do not earn Social Security benefits. It is a defined benefit plan in which the government promises a specified monthly pension. FERS was established on January 1, 1987, for all employees hired since December 31, 1983. The program has three components: a defined benefit or pension, a defined contribution plan in which the employer and employee make regular contributions, and Social Security benefits. The Middle Class Tax Relief and Job Creation Act of 2012¹⁷ requires new employees hired on or after January 1, 2013, to be covered under FERS as revised annuity employees (RAE). These RAEs must pay 3.1 percent of their salary as FERS retirement contributions. This is a 2.3 percent increase over what employees hired before January 1, 2013, must pay. Additionally, the Bipartisan Budget Act of 2013 increased that contribution to 4.4 percent for RAEs hired on or after January 1, 2014.

The Postal Service's retirement expense was 12.3 percent of total compensation and benefits expenses in FYs 2012 and 2013, and 12.2 percent in FY 2011. In the private sector, retirement and savings benefits average 3.7 percent of total compensation and benefits expenses. For state and local governments, retirement and savings benefits average 9.4 percent.

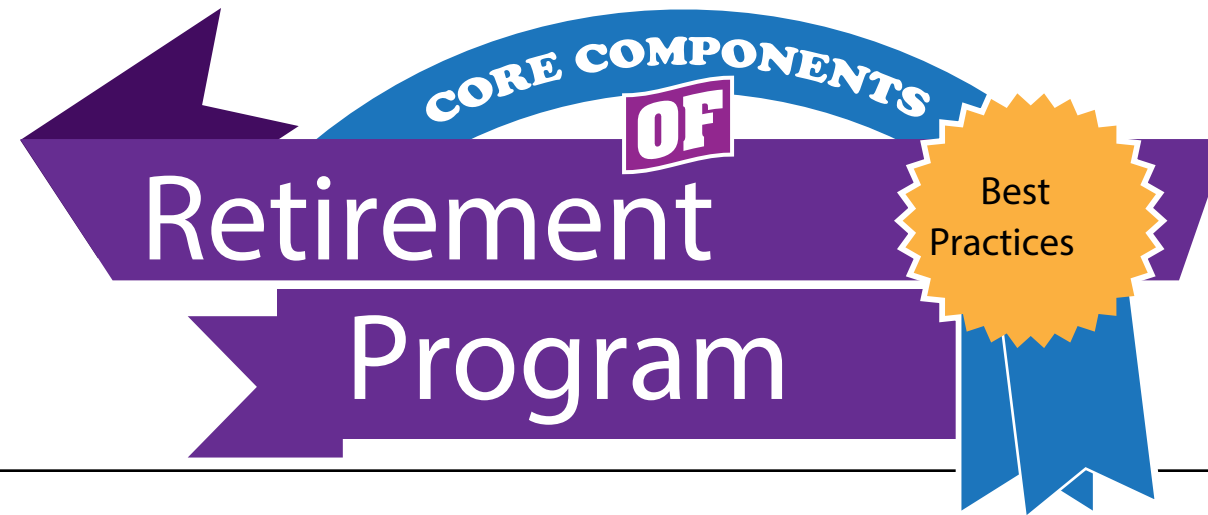
Defined benefit plans, such as pensions, generally pay a guaranteed sum based on the employee's wages and years of service. In contrast, a 401(k) plan (as well as the 403(b) plan)¹⁸ is a defined contribution plan, which means the money the employee receives in retirement is based on the money the employee (and the employer, if there is a match available) contributed to the plan. The 401(k) plans give employees automatic deductions from paychecks, pretax incentives, matching programs, and control over their own investments.

¹⁵ Title 39 U.S.C. § 1005(d)(1).

¹⁶ Title 39 U.S.C. § 1003(a).

¹⁷ Public Law 112-96 § 5001, February 22, 2012.

¹⁸ A 401(k) plan is a tax-qualified, defined-contribution pension account defined in subsection 401(k) of the Internal Revenue Code. A 403(b) plan is similar to a 401(k) plan but is available for public education organizations, some nonprofit employers, cooperative hospital service organizations, and self-employed ministers.



**Roll over the each category to
reveal the best practice information**

Private company and public sector retirement plans have undergone significant changes over the past 20 to 30 years. Pension plans used to be the most common form of retirement program in the U.S., but recently 401(k) plans have become more popular. Benchmarked organizations are phasing out costly pension programs and implementing 401(k) matching programs that place the employee in control of his or her financial future and shift the responsibility of retirement from the organization to the employee. According to the postmaster general, it is urgent that the Postal Service implement strategies now to improve its position presently and in the future. Additionally, he stated a defined contribution retirement system for future employees would help ensure the Postal Service can fulfill its obligations not only to future employees but to retirees and current employees as well.

Current Postal Service Retirement Benefits Program

The Civil Service Retirement Act of 1920 established CSRS for certain federal employees. It was replaced by FERS for federal employees hired on or after December 31, 1983. CSRS is a defined benefit, contributory retirement system. Employees contribute between 7 and 8 percent of their pay to the CSRS and the employing agency matches that contribution. It provides a basic annuity upon retirement based on length of service and a percentage of an average of the highest average basic pay¹⁹ earned during any 3 consecutive years of service. Employees also receive credit for any unused sick leave if they retire on an immediate annuity.²⁰ Employees covered by CSRS do not pay Social Security payroll taxes and they do not earn Social Security benefits. They may increase their earned annuity by contributing up to 10 percent of basic pay to a voluntary contribution account or to the Thrift Savings Plan (TSP).²¹ There is no government contribution but employee contributions are tax-deferred.

FERS provides benefits from three sources: a basic benefit plan, Social Security benefits, and TSP. The basic annuity is calculated based on length of service and a percentage of an average of the highest basic pay earned during any 3 consecutive years of service.²² Employees contribute 0.8 percent of their salary towards their FERS pension. The Middle Class Tax Relief and Job Creation Act of 2012 requires new employees hired on or after January 1, 2013, to be covered under FERS as RAEs. These new employees must pay 3.1 percent of their salary as FERS retirement contributions. This is an increase of 2.3 percent over what employees hired before January 1, 2013, had to pay. Additionally, the Bipartisan Budget Act of 2013 increased that contribution to 4.4 percent for new employees hired on or after January 1, 2014.

The TSP is a defined contribution plan. The retirement income from TSP will depend on how much an employee and employing agency contribute to an employee's account during his or her working years and the earnings accumulated over that time. Even if employees do not contribute to a TSP account, employing agencies automatically contribute 1 percent of basic pay for every FERS employee hired before August 1, 2010. For FERS employees hired on or after that date, the employing agency automatically contributes 3 percent. Employees can also voluntarily contribute additional amounts from their basic pay until they reach the Internal Revenue Code contribution limit,²³ and employing agencies match the first 5 percent of those contributions.²⁴ If employees stop contributing, the agency matching contributions will also stop, but the agency's automatic contributions will continue.

¹⁹ Basic salary earned for that position. It includes increases in salary for which retirement deductions are withheld. It does not include payments for overtime or bonuses.

²⁰ An immediate retirement benefit is one that starts within 30 days of the date an employee stops working.

²¹ The TSP is a retirement savings and investment plan established by Congress in the Federal Employees' Retirement System Act of 1986.

²² One percent of high-3 average salary for each year of service for employees under age 62 at retirement; or age 62 or older at retirement with less than 20 years of service. The benefit increases to 1.1 percent at age 62 or older at retirement with 20 or more years of service. Special provisions also apply for air traffic controllers, firefighters, law enforcement officers, capitol police, and nuclear materials couriers.

²³ \$17,500 for calendar year 2014. Amounts may be deducted before taxes are withheld (traditional contributions) or after taxes have been withheld (Roth contributions).

²⁴ The first 3 percent is matched dollar-for-dollar by the employing agency. The next 2 percent is matched at 50 cents on the dollar. This means that when employees contribute 5 percent of basic pay, the employing agency contributes another 4 percent of basic pay to the TSP account. Together with the agency's automatic contribution (1 percent), the employing agency puts in a total of 5 percent. Employing agencies only match the first 5 percent of employee contributions.

We focused on how the organizations structure their retirement benefits, changes made to those benefits, and the corresponding reasons for the changes.

Newly hired federal employees who already have tax-deferred money in a traditional individual retirement account or another eligible employer plan can transfer those accounts into their TSP. Conversely, workers who leave the federal government can transfer their TSP funds on a tax-deferred basis into another tax-qualified retirement savings account. Postal Service employee contribution rates to the TSP program average between 4 and 4 1/2 percent of pay.

To ensure the Postal Service can guarantee defined benefits under the FERS program, the Office of Personnel Management (OPM) requires the Postal Service to fund the cost through:

- Total Normal Cost. This is the cost of projected retirement benefits allocated to the current year. The OPM determines this cost, which is offset by employee contributions to the plan.²⁵
- Additional payment if OPM determines that FERS plan liabilities exceed assets.²⁶

Ideally, all benefits are funded through the total normal cost. However, when interest rates decline as they have over the past several years, the overall value of the FERS plan declines, and those guaranteed benefits become unfunded. As such, to ensure defined benefits, the OPM increases the total normal cost so the Postal Service's overall funding cost increases.

Retirement Benefits Benchmarking Snapshot

We benchmarked with eight organizations across the education, communications, parcel, postal, energy, and insurance industries as well as the government sector. Two of the eight organizations have unionized workforces and all of the private companies operate nationwide. We focused on how the organizations structure their retirement benefits, changes made to those benefits, and the corresponding reasons for those changes. All eight organizations historically had traditional pension plans. However, seven of them transitioned, at least partially, to a 401(k) or 403(b) defined contribution retirement benefits plan. The state organization maintained a traditional pension plan, but it increased the retirement age requirement, decreased the percentage of employee benefits, and offered a delayed compensation plan. See Table 1 for a snapshot of retirement benefits for the private and government sector benchmarked organizations.




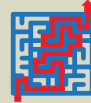

Also, the Dutch government established a defined-ambition program, which keeps the idea of an employer promise but loosens the bonds of that promise.²⁷ Employers try to pay a specific pension, but unlike defined benefit pension programs, defined-ambition programs permit the employer to lower the pensions if it is unable to deliver on its promise. It is a soft promise that aligns the focus of the company and the employee on achieving an adequate pension.

²⁵ Employees hired before January 1, 2013, must pay .8 percent of their salary as FERS retirement contributions. New employees hired on or after January 1, 2013, must pay 3.1 percent and employees hired on or after January 1, 2014, must pay 4.4 percent.

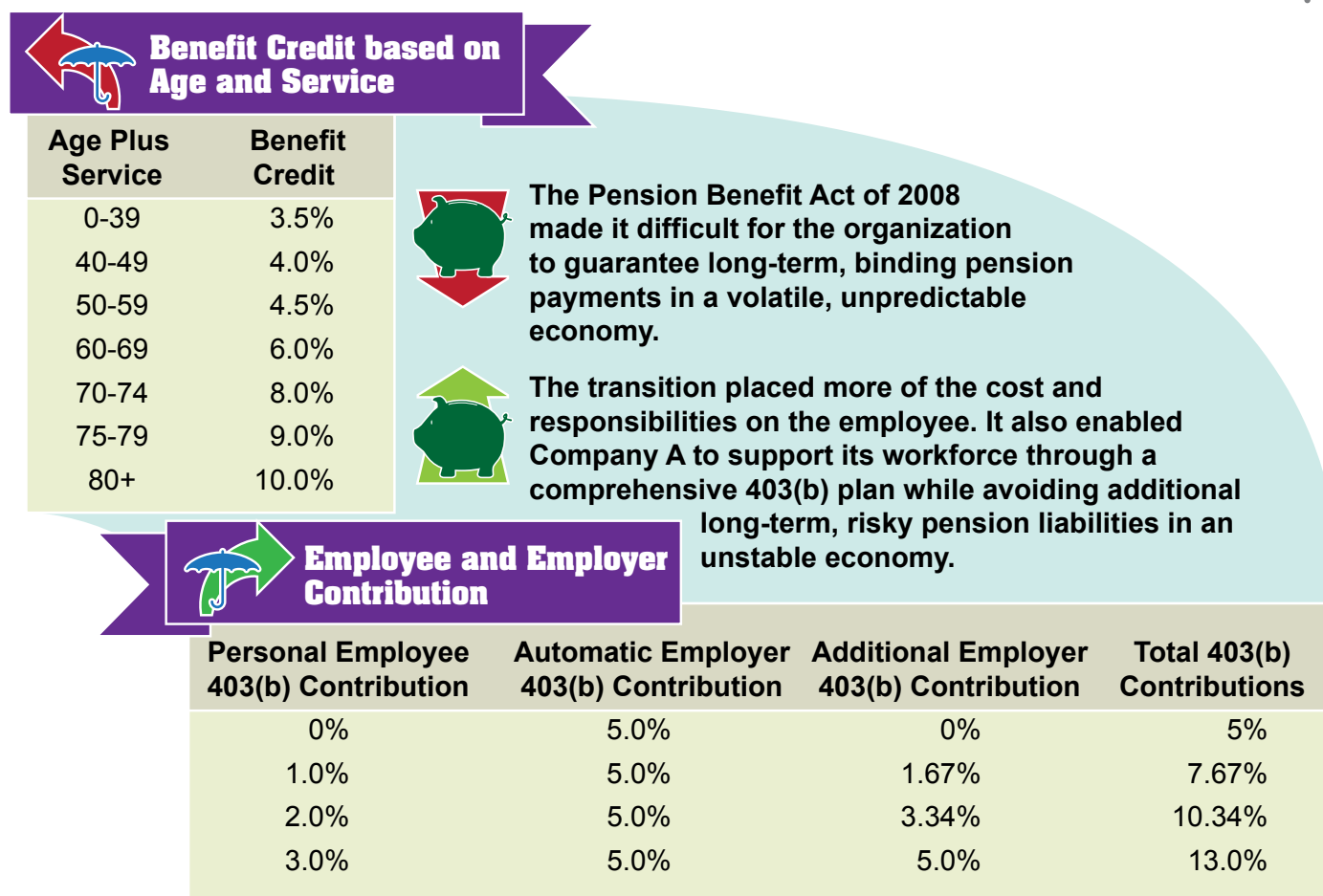
²⁶ Since 1985, FERS plan assets have exceeded liabilities so this portion of the funding requirement does not currently apply.

²⁷ None of the benchmarked companies transitioned to a defined-ambition program.

Table 1. Benchmarked Organizations' Retirement Benefits Program Comparison

 Benchmarked Organization	 Previous Retirement Benefits Program	 Current Retirement Benefits Program	 Challenges	 Results
Company A (Public) Academic and Research Institution	Pension Defined Benefit Program	403(b) Defined Contribution Program	Stringent regulations; binding pension payments	Avoid risky pension liabilities in unstable economy
Company B (Private) Communications	Pension Defined Benefit Program	401(k) Defined Contribution Program	Defined benefit pension plan commitment exceeded assets	Cut long-term, binding pension liabilities and save over \$3 billion between 2006 and 2016
Company C (Private) Package Delivery, union and nonunion workforce	Pension Defined Benefit Program	401(k) Defined Contribution Program (non-unionized employees); Pension Defined Benefit (unionized employees)	Mounting pension debt and future payment obligations	Established portable account formula so employees can maintain retirement savings upon moving
Company D (State)	Pension Defined Benefit Program in Replace of Social Security	Same; Adjusted Retirement and Time-at-organization requirements. Offered delayed compension plan.	Mounting pension debt; fraud	Projected to save \$5 billion over 30 years
Company E (City)	Pension Defined Benefit Program	Hybrid Pension Defined Benefit and 401(k) Defined Contribution plan (in process)	High pension costs in unstable economy	Offer employees multiple options to save while limiting burdensome pension costs
Company F (Private Postal) Physical and Electronic Delivery, unionized workforce	Pension Defined Benefit Program	401(k) Defined Contribution Program	Unmanageable pension liabilities due to weak economy and extended average retirement period.	Share retirement savings responsibility; allow employees to earn retirement savings while moving between jobs
Company G (Private) Energy	Pension Defined Benefit Program	401(k) Defined Contribution Program	Difficult to maintain long-term, binding pension liabilities due to unstable economy and volatile interest rates	Eliminate long-term, binding pension liabilities.
Company H (Private) Insurance	Pension Defined Benefit Program	Hybrid Pension Defined Benefit and 401(k) Defined Contribution plan	Difficult to guarantee promised pension benefits due to unstable economy and unpredictable interest rates	Decreased long-term pension liabilities; more savings responsibility on employee; less risk; more employee freedom and flexibility.

Source: Contractor's retirement benefits comparative analysis.



Source: Company A, Office of Faculty and Staff Benefits.
Source: Contractor's retirement benefits comparative analysis.

Company A

Company A is one of the world's leading academic and research institutions. Before 2008, Company A offered a traditional pension plan. As shown in [Table 2](#), employees started with a cash balance of zero and automatically received a savings payment towards their pension based on age plus years of service.

Table 2. Benefit Credit Based on Age and Service

Age Plus Service	Benefit Credit
0-39	3.5%
40-49	4.0%
50-59	4.5%
60-69	6.0%
70-74	8.0%
75-79	9.0%
80+	10.0%

Source: Company A, Office of Faculty and Staff Benefits.

In addition to the automatic employer contribution, employees also received an annual interest credit that varied based on the market's health. However, the rules and regulations in the Pension Benefit Act of 2008 made it difficult for Company A to control its pension program and challenged its ability to guarantee long-term, binding pension payments in a volatile, unpredictable economy. As a result, Company A transitioned to a 403(b) plan for all employees hired after January 1, 2009. As shown in Table 3, Company A now automatically contributes 5 percent of employee gross pay, regardless of whether employees contribute. Company A also contributes an additional 5 percent when the employee contributes 3 percent of his or her salary.

Table 3. Sample Employee and Employer Contribution

Personal Employee 403(b) Contribution	Automatic Employer 403(b) Contribution	Additional Employer 403(b) Contribution	Total 403(b) Contributions
0%	5%	0%	5%
1%	5%	1.67%	7.67%
2%	5%	3.34%	10.34%
3%	5%	5%	13%

Source: Contractor's retirement benefits comparative analysis.

This transition placed more of the cost and responsibilities on the employee. It also enabled Company A to support its workforce through a comprehensive 403(b) plan while avoiding additional long-term, risky pension liabilities in an unstable economy.

Company B

Company B is a global leader in innovative communications and technology solutions and has a unionized workforce. Before 2006, Company B offered a traditional pension plan in which all employees received pension payments based on their age and years of service. In 2006, the company froze all pension payments and transitioned to a 401(k) plan. Employees continue to receive the pension benefits they have earned throughout their career but do not accumulate additional savings moving forward. Under the new plan, Company B matches 100 percent of employee contributions up to 6 percent of their salary. Even with the freeze, by the end of 2010, Company B's defined-benefit pension plan had \$27 billion in commitments yet only \$18 billion in assets. Also, due in part to higher post-retirement costs, Company B experienced \$16 billion in pension-related charges from 2010 to 2013. Still, Company B expects its decision to freeze all pension payments will save more than \$3 billion between 2006 and 2016.

Company C

Company C is the world's largest package delivery company and a leading global provider of specialized transportation and logistics services. It has both unionized and nonunionized employees. Before 2008, Company C offered a traditional pension plan for all employees. However, as shown in Table 4, Company C transitioned its nonunionized workforce hired on or after January 1, 2008, to a 401(k) plan to reduce mounting pension debt and future payment obligations.

Table 4. Unionized and Nonunionized Employees Retirement Benefits

	Date Hired	401(k) Plan	Pension Plan
Unionized Employees	Before January 1, 2008	x	✓
	On or After January 1, 2008	x	✓
Nonunionized Employees	Before January 1, 2008	x	✓
	On or After January 1, 2008	✓	x

Source: Contractor's retirement benefits comparative analysis.

Although Company C maintained its pension plan for unionized employees, it extended its "time at the organization" requirement from 25 to 30 years.²⁸ It also established a portable account formula to appeal to a more mobile, transient workforce. Specifically, Company C shortened the vesting period required for unionized employees to start receiving pension funds upon retirement. After 3 years, unionized employees are entitled to a certain percentage of pension funds so they can remain flexible and mobile while still saving money for retirement. While negotiations continue, the union prefers a pension plan as it guarantees retirees an established steady, reliable source of income upon retirement. However, under the new 401(k) retirement match plan, nonunionized employees have access to "free money" and the ability to increase their pretax retirement contributions. More specifically, nonunionized employees are able to contribute an unlimited percentage of their income towards retirement savings and Company C will match 100 percent of their contributions up to 3.5 percent. Union members, on the other hand, are limited to the set pension rate and are unable to add pretaxed contributions towards their retirement savings. Moving forward, Company C plans to persuade all employees that the 401(k) is the best retirement benefits program for the organization to free itself of long-term costly payments.

²⁸ Company C required its employees to work at the organization for at least 25 years before they could retire and begin to receive full, unpenalized pension benefits.

Company D

Company D, a state government, uses a traditional pension plan in place of Social Security benefits. As shown in Table 5, employees automatically contribute a percentage of their income towards the state retirement system based on their hire date.

Table 5. Retirement Benefit Contribution Based on Date Hired

Date Hired	Employee Retirement Benefit Contribution Rate
Before January 1, 1975	5%
January 1, 1975, through December 31, 1983	7%
January 1, 1984, through June 30, 1996	8%
July 1, 1996, to the Present	9%

Source: Contractor's retirement benefits comparative analysis.

Upon retirement, employees receive payments from a pension account based on age, years of service, average of the 3 highest consecutive years' salaries, and group classification.

To modernize its pension plan and limit associated costs, Company D maintained the traditional pension plan structure but increased the retirement age from 60 to 67 and increased years of service requirements. Finally, it established a no-spiking rule to limit annual salary increases that count towards a pension to no more than 7 percent of the average earnings over the last 2 years plus inflation. Company D hopes to save \$5 billion over the next 30 years with this pension plan.

In addition to the pension program, Company D also offers its employees a delayed compensation plan to provide an alternative retirement savings vehicle and encourage state employees to fully plan and prepare for retirement. The state allows employees to set aside additional pretax retirement savings. While there is no match, upon retirement employees can access their individual contributions in addition to their pension payments.

Company E

Company E, an independent city, offered a traditional pension plan to its employees. However, over the past 5 years, Company E has been transitioning to a hybrid pension and 401(k) plan to parallel its state's retirement benefits. As shown in Table 6, employees hired before December 31, 2009, are part of a pension program based on an employee's age, years of credible service, and an average of the last 36 consecutive months of compensation. Employees hired between January 1, 2010, and December 31, 2013, are part of a plan very similar to the previous one but the qualifications for full retirement benefits increased from age 65 with 5 years of credible service (or age 50 with at least 30 years of service) to age and years of service that equal 90. Employees hired after January 1, 2014, are part of a hybrid pension and 401(k) plan.

Table 6. Key Facts on City/State Retirement System

	Retirement System 1	Retirement System 2	Retirement System 3
Eligible members	Hired before December 31, 2009	Hired between January 1, 2010, and December 31, 2013	Hired January 1, 2014, or after
Retirement contribution	5 percent	5 percent	Combination of mandatory and voluntary employer and employee contributions
Type of plan	Pension program based on age, years of credible service, and salary	Similar to retirement system 1	Hybrid pension defined benefit and 401(k) defined contribution plan (in process)
Retirement age	65	Social Security retirement age	Social Security retirement age
Earliest unreduced retirement eligibility	Age 65 with at least 5 years of credible service	When employee's age and credible service equal 90	When employee's age and credible service equal 90

Source: Contractor's retirement benefits comparative analysis.

According to company officials, the hybrid retirement plan combines the features of a defined-benefit plan, which pays a monthly retirement benefit, and a defined contribution plan, which provides a retirement benefit based on contributions to the plan and the investment performance of those contributions. Through a hybrid retirement benefits program, Company E can offer its employees multiple options to save for retirement while limiting burdensome pension costs. Specifically, Company E combined both retirement programs to create a more sustainable program for both the employee and employer. With a hybrid retirement plan, Company E decreased the pension payments and limited its debt while still providing its employees guaranteed payments upon retirement and allowing them to set aside additional funds as retirement savings before being taxed.

Company F

Company F is a world leader in providing innovative physical and electronic delivery solutions and has a unionized workforce. It offers a traditional pension plan to its entire workforce. Employees are eligible to receive unreduced benefits as soon as they reach the age of 55 and have more than 30 years of credible service at the organization. However, Company F has accumulated unmanageable pension liabilities because of a weak economy and an extended average retirement period. By the middle of 2014, Company F will have more than \$1 billion in pension payment obligations to its retired workforce. As a result, Company F is undergoing a major retirement benefits transition to limit costs associated with its pension program. Although the union is predominantly in favor of the traditional pension plan, Company F plans to offer a 401(k) plan to all employees hired after a certain date. The 401(k) plan is intended to share the burdens of a retirement benefits plan with the employee through a comprehensive 401(k) matching plan.

Company G

Company G is one of the nation's largest producers and transporters of energy. Before 2008, Company G offered a traditional pension plan to attract and retain talented employees within the organization. However, the company found the plan difficult to maintain because of an unstable economy and volatile interest rates. As a result, Company G transitioned to a 401(k) plan for all employees hired after 2008. Employees that remain enrolled in the traditional pension plan may also participate in the 401(k) program but have a much smaller match component than those enrolled in the newer 401(k) plan.

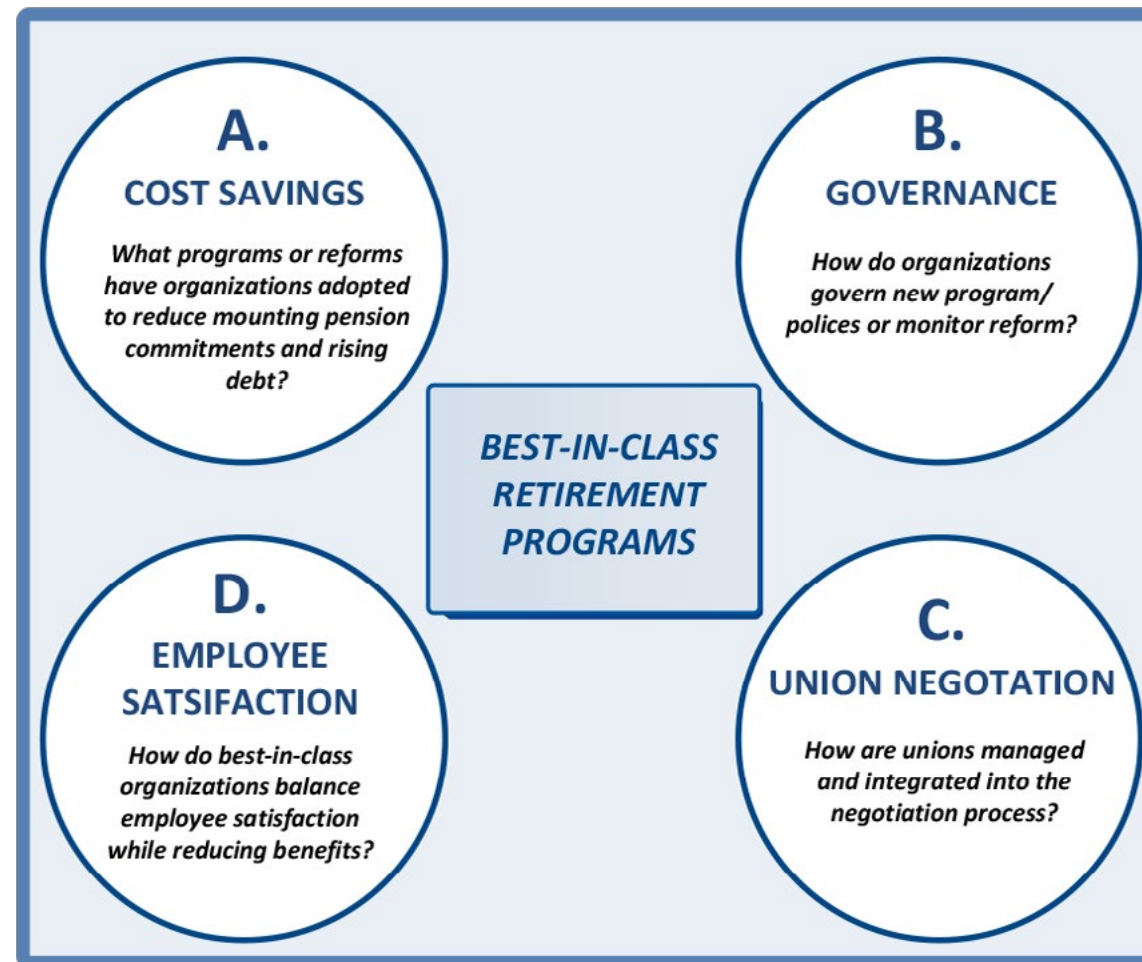
By using a 401(k) match plan rather than a pension plan, Company G can still contribute to employees' retirement while eliminating long-term, binding pension liabilities.

Company H

Company H is the number one provider of guaranteed-renewable insurance in the U.S. Before 2008, Company H offered a traditional pension plan to its employees. However, Company H faced mounting debt as its pension liabilities grew out of control. In an unstable economy with unpredictable interest rates, Company H found it difficult to guarantee retirees the pension benefits they were promised. Company H recently restructured its retirement benefits program and now offers a combination of a pension and a 401(k) retirement plan. It decreased pension benefits and introduced a comprehensive 401(k) matching program. Employees hired after 2008 receive a 50-percent employer match of all personal 401(k) contributions up to 6 percent of their salary and receive unreduced pension payments as soon as their years of credible service and age add up to 80. By offering a hybrid retirement plan, Company H decreased the amount of long-term pension liabilities and put more retirement savings responsibilities on the employees. Further, the organization faces less risk while the employee has more freedom and flexibility to contribute to his or her own retirement savings.

Common Practices

We identified a set of common practices recognized by benchmarked companies and organizations when considering retirement benefits plans. As shown in Figure 1, these practices involve strategies in four areas:



The Postal Service should consider these practices if it pursues any changes to its retirement benefits programs. See [Appendix A](#) for additional details on these common practices.

Benchmarked companies reported savings from about \$1 billion to about \$5 billion; one private company projected to save about \$3 billion over 10 years, and another company projected to save \$5 billion over 30 years.

Conclusion

Pensions, which were originally intended to attract and retain talented employees, are a major cost to organizations and may be less important as workers become more mobile and transient throughout their careers. Pension payments are becoming larger as the retirement window continues to grow with increasing life expectancy. In a volatile economy, many organizations are unable to meet their promised pension payments as they struggle to maintain an adequate rate of return on their assets. However, many unions and employees still demand a pension plan. Many organizations are adjusting their retirement benefits programs to cater to an evolving workforce while alleviating long-term retirement costs. Figure 2 shows the risks associated with each retirement benefits program.

Figure 2. Risk Profile of Pension Systems



Source: Contractor's analysis.

Many organizations are transitioning towards a 401(k) plan and matching a certain percentage of employee 401(k) contributions to collaboratively invest towards an employee's retirement. Further, organizations have created hybrid retirement benefits programs when a full transition to a 401(k) plan is not feasible. Hybrid plans offer both a pension and 401(k) plan. The Dutch government also established a defined-ambition program which keeps the idea of an employer promise but loosens the bonds of that promise. Employers try to pay a specific pension, but unlike defined benefit pension programs, defined-ambition programs permit the employer to lower the pensions if it is unable to deliver on its promise. It is a soft promise that aligns the focus of the company and the employee on achieving an adequate pension.²⁹ Organizations that maintained their traditional pension programs often reduced the benefits or adjusted the minimum age an employee can retire and receive retirement benefits without penalty. Benchmarked companies reported savings from about \$1 billion to about \$5 billion, including one private sector company that projected savings of about \$3 billion over 10 years and one that projected savings of \$5 billion over 30 years.

²⁹ We did not identify any organizations in the U.S. that adopted a defined-ambition pension program.

Appendix A: Common Practices

Cost-Saving Program Strategy

A cost-saving program strategy looks at the fiscal aspect of retirement benefits plans. Successful cost-saving program strategies consider the most realistic, economically sustainable program for the employer as well as overall employee satisfaction. Common practices include:

- Maintaining pension plan structure to satisfy union preferences but introducing reforms to reduce pension liabilities and debt, including:
 - Increasing the retirement age eligibility requirement to account for longer life expectancy.
 - Increasing the time at the organization eligibility requirement to reduce pension payments.
 - Transitioning away from “Rule of 85”³⁰ to leverage experienced employees for a longer period.
- Transitioning towards a 401(k) retirement benefits plan to avoid high-risk pension plans.
- Freezing pension plans while transitioning to a 401(k) benefits program to prevent increasing debt.
- Introducing 401(k) matching programs to relieve organizations from costly pension plans.
- Creating a hybrid plan to leverage best practices from pensions and 401(k) retirement plans.

Governance and Administration

The right leadership and administrative personnel, both in-house and third party, are critical to proper oversight, development, or reform of a retirement benefits program to ensure it meets the needs of the employer and the employee. Common practices include:

- Hiring finance and accounting subject matter experts to oversee internal operations and coordinate with third-party vendors.
- Partnering with third-party vendors to manage investments, risks, and regulatory requirements associated with retirement benefits programs.
- Using a data management system to ensure payroll compliance and limit fraud (for example, making sure the right person receives the pension payment, and that pension payments do not continue after the recipient has passed away).
- Creating a web portal to increase employees’ access and visibility to their retirement benefits program.
- Transitioning away from pension plans to defined contribution plans to avoid large costs and administrative burdens associated with the Pension Protection Act.
- Establishing a dedicated office to support employee inquiries and concerns.

³⁰ An employee receives his or her full pension benefits once years of service and age add up to 85.

Union Negotiations and Relations

A healthy, collaborative relationship between the organization and its unions is pivotal to ensuring a productive, efficient reform process that results in a retirement benefits program that is ideal for the employer and the employee. Organizations should be transparent and consider union stance during all stages. Common practices include:

- Maintaining an open dialogue between management teams and unions on pension reform to ensure healthy collaboration.
- Establishing a joint committee of union and organization leaders to facilitate diplomatic negotiations.
- Openly communicating pension difficulties and cost burdens with unions to encourage negotiation and collaboration.
- Balancing relationships with multiple unions to satisfy retirement benefits for all parties involved.
- Offering attractive 401(k) matching plans for nonunionized employees to persuade unions to move away from a traditional pension plan.

Employee Satisfaction

Employers must customize a retirement benefits program that satisfies the employees who are ultimately going to receive retirement benefits. Common practices include:

- Offering a portable retirement benefits account to appeal to a younger and more mobile workforce.
- Implementing cost-of-living adjustments for all retirees to account for an increasing consumer price index.
- Creating a 401(k) matching scale that attracts, retains, and rewards employees based on tenure or performance.
- Establishing alternative ways for employees to invest personal savings towards retirement outside of traditional pension plans.



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